



MAINE REVENUE SERVICES GUIDANCE ON THE PINE TREE DEVELOPMENT ZONE INCOME TAX CREDIT

36 MRSA § 5219-W

The Pine Tree Development Zone (“PTDZ”) income tax credit is available to certified businesses engaged in qualified activity for tax years beginning on or after January 1, 2004. The credit is available to all businesses (corporations, pass-through entities, or sole proprietorships) certified by the Department of Economic and Community Development (“DECD”). To obtain certification, the business must apply to DECD and meet the requirements for qualified business activity.

1. Application for Certification as set forth in DECD Rule 19-100 §6(2)

An application for certification made by a business that plans to enter or expand into a Pine Tree Development Zone shall contain the following information for the business, including all of its affiliates within the state:

A. Descriptive data:

- (1) A description of the business, its products and/or services and history of operation;
- (2) A description of the business operations or activities that will be conducted within the Pine Tree Development Zone;
- (3) A description of the market(s) and/or competitive environment in which the business operates or expects to operate; and
- (4) A description of the employment growth and investment plans for the business within a Pine Tree Development Zone over the five years following the date of application, including:
 - a. Facilities to be constructed or modified;
 - b. Equipment to be purchased;
 - c. Number and average wages of new, full-time employees to be hired; and

d. Number and average wages of part-time employees to be hired;

B. Base level data:

(1) Employment, including:

- a. The number and location of all employees employed within the state by the business and its affiliated businesses as of the December 31st preceding its certification; and
- b. The number and location of qualified employees of that business on each of 6 consecutive measurement days in each of the 3 calendar years in the base period preceding its certification as chosen by the business divided by 18;¹

(2) Total payroll within the state of the business for each of the three calendar years preceding its certification; and

(3) Total Maine state income taxes withheld for employees of the business for each of the three calendar years preceding its certification;

C. A statement describing the basis under which it has been determined that the project would not go forward but for the benefits provided by the Pine Tree Development Zone program; and

D. Certification that at least one of the new employees to be employed, within the Pine Tree Development Zone will be:

(1) Paid a wage that, when calculated on a calendar year basis, exceeds the average per capita wages in the county in which employed;

¹ In order to ensure a more accurate measure of employment, DECD is proposing a change to this subparagraph, to be applied retroactively, to redefine the measurement days to be the last day of each quarter during the calendar year.

(2) Offered participation in a retirement program subject to the Employee Retirement Income Security Act of 1974, 29 U.S.C. §§1001-1461; and

(3) Offered participation in a group health insurance plan.

Once this information is provided, it is reviewed by DECD. For the “but for” statement under paragraph C above, DECD provides an advisory opinion regarding whether or not the business has met the requirements of the “but for” test and the final determination is made by Maine Revenue Services. After the “but for” test is approved, DECD makes a determination regarding overall qualification.

2. Requirements for Certification

In order to be certified, a business must satisfy the following requirements:

A) The business must be engaged in a targeted business sector (manufacturing, financial services, selected technologies);

1) Selected technologies include biotechnology, aquaculture and marine technology, composite materials technology, environmental technology, advanced technologies for forestry and agriculture, information technology and precision manufacturing technology;

B) The business must intend to expand the base level of employment with qualified employees. The base level of employment means the greater of the number of employees in Maine on December 31 of the year immediately preceding certification or the average number of employees over the three calendar years preceding certification. If a business has affiliates, the number of employees of the affiliates is included in the base level of employment; and

C) Qualified employees must meet the requirements of certification listed above as well as being new full-time employees who are residents of Maine and are hired by a Pine Tree Development Zone business for work directly in one or more qualified business activities.

3. Years Tax Credit is Available

Once certified, a business may be able to claim the income tax credit for ten years, beginning with the year in which the business actually commences qualified business activities.

4. Priority of PTDZ Credit over other Credits

Because the credit is based on tax liability in a given tax year, there is no provision for carrying forward the credit to future years. Taxpayers, however, may apply the PTDZ credit against tax liability before utilizing any other available credit. For example, if a taxpayer has current year Maine tax liability of \$100,000, a PTDZ credit of \$75,000 (75% of liability), and a High Tech credit of \$50,000 (which may be carried forward 5 years), the taxpayer can reduce tax liability by \$75,000 with the PTDZ credit, and then reduce the remaining tax liability to zero by applying \$25,000 of the \$50,000 High Tech credit. The remaining \$25,000 in High Tech credit may be carried forward.

5. Determination of Credit Amount

The credit is based on the tax liability related to income from qualified PTDZ business activity. For the first 5 years, the credit is equal to 100% of the tax liability; for the next 5 years it is equal to 50% of the tax liability. Certified business entities that have both qualified and non-qualified business activity are allowed a credit for only a portion of the total tax liability. To determine the percentage of tax that is allowed as a credit, the business must divide the total value of property used and payroll paid during the year that was directly related to qualified activity by the total value of all Maine property used and Maine payroll paid in the year. This process is also called apportionment and is described in detail in

the following section. The credit percentage is then applied against the total tax liability to determine the dollar amount of the credit. (See credit application worksheet).

6. Apportionment

The apportionment statute appears in Title 36, section 5219-W, as follows:

2. Apportioned credit in certain circumstances. In the case of a qualified Pine Tree Development Zone business, as defined in Title 30-A, section 5250-I, subsection 17, that has a business presence in the State other than that conducted within a Pine Tree Development Zone, as defined by Title 30-A, section 5250-I, subsection 13, including, but not limited to, a qualified Pine Tree Development Zone business that is required to file a combined report pursuant to Title 36, section 5220, subsections 5 and 6, the Maine income tax liability of the qualified Pine Tree Development Zone business, and the affiliated members of its unitary group, if any, upon which the credit provided for in this section must be calculated based upon a pro forma determination. The pro forma determination must be based on the assumptions that all of the business activities conducted by the qualified Pine Tree Development Zone business and the affiliated members of its unitary group, if any, within this State constitute a unitary business and that only the qualified business activity conducted in the Pine Tree Development Zone is subject to tax imposed by this chapter. *The portion of the tax liability of the qualified Pine Tree Development Zone business and the affiliated members of its unitary group, if any, related to the business activity conducted in the Pine Tree Development Zone must be determined by use of a percentage, the numerator of which is the property value and the payroll for the taxable year directly attributed to the qualified business activity of the business and the denominator of which is the statewide property value and payroll for the taxable year of the qualified business and the members of its unitary group.*

“[Q]ualified business activity” means only the activity associated with the expansion or initial business creation for which the entity has been certified by DECD (*see* 30-A MRSA § 5250-I(16) & (17)).

Therefore, a taxpayer that has business income from both PTDZ qualified business activity and non-qualified business activity is allowed a tax credit for the tax associated with only the income generated by the qualified business activity.

The determination of property values and payroll generally follows the methods and definitions that are used for multi-state corporate income tax apportionment under 36 M.R.S.A. § 5210-11 and MRS Rule 801.06 and .07.

Apportionment Factor. The apportion factor is a fraction used to calculate the ratio of qualified to non-qualified business. The numerator of the apportionment factor is the average value of the taxpayer's real and tangible personal property used in a qualified business activity during the taxable year plus the total amount paid during the tax year by the taxpayer for compensation to employees engaged in a qualified activity. The denominator of the apportionment factor is the average value of all the taxpayer's real and tangible personal property used during the tax year in Maine plus the total compensation paid for all Maine employees during the tax year. A business may not include in the numerator property or payroll related to transfers to the zone from elsewhere in Maine (*see* 30-A MRSA §§ 5250-J(3)(C) & (D)).

A. Real and Tangible Personal Property. The term "real and tangible personal property" includes land, buildings, machinery, stocks of goods, equipment, and other real and tangible personal property but does not include coin or currency.

B. Property Used During the Taxable Year. Property is included in the apportionment factor if it is actually used or is available for or capable of being used during the tax period by the taxpayer. Property held in reserve or standby facilities or property held as a reserve source of materials must be included in the factor. For example, a plant temporarily idle or raw material reserves not currently being processed are includable in the factor. Property or equipment under construction during the tax period (except inventoriable goods in process) must be excluded from the factor until such property is actually used by the taxpayer. If the property is partially used in Maine by the taxpayer while under construction, the value of the property to the extent used must be included in the apportionment factor. Property used in Maine by the taxpayer must remain in the apportionment factor until its permanent withdrawal is established by an identifiable event

such as its sale, or the lapse of an extended period of time (normally, five years) during which the property is held for sale.

C. Property in transit/Mobile property. Property in transit between locations of the taxpayer to which it belongs is considered to be located at the destination for purposes of the apportionment factor. Property in transit between a buyer and seller that is included by a taxpayer in the denominator of its apportionment factor in accordance with its regular accounting practices must be included in the numerator according to the site of destination (PTDZ or non-zone). The value of mobile or movable property, such as construction equipment, trucks, or leased electronic equipment that is located both within and without a Pine Tree Development Zone during the taxable year, is determined for purposes of the numerator of the apportionment factor on the basis of total time within the zone during the taxable year. Automobiles assigned to traveling employees are included in the numerator of the factor of the site to which the employee's compensation is assigned under the payroll segment of the apportionment factor.

D. Valuation (owned property). Property owned by the taxpayer is valued at its original cost. "Original cost" means the basis of the property for federal income tax purposes (prior to any federal adjustments) at the time of acquisition by the taxpayer and adjusted by subsequent capital additions or improvements thereto and partial disposition thereof, by reason of sale, exchange, abandonment, etc. However, capitalized intangible drilling and development costs are included in the factor whether or not they have been expensed for either federal or state tax purposes. If the original cost cannot be ascertained, the property must be included in the factor at its fair market value as of the date of its acquisition by the taxpayer.

Generally, the average value of property owned by the taxpayer is determined by averaging the values at the beginning and ending of the tax period. However, the State Tax Assessor may require or allow averaging of monthly values if substantial fluctuations in the values of the property exist during the taxable year or if property is acquired after the beginning of the taxable year or disposed of before the end of the taxable year.

E. Valuation (rented property). Property rented by the taxpayer is valued at 8 times the net annual rental rate. Subrentals are not deducted. If property is used at no charge or rented for a rate other than a reasonable market rate, the property must be included in the apportionment factor on the basis of a reasonable market rental rate. The "annual rental rate" is the amount paid as rent for the property for a twelve-month period. Where property is rented for less than a twelve-month period, the net rent paid for the actual period of rental constitutes the "annual rental rate" for the tax period. However, where a taxpayer has rented property for a term of 12 or more months and the current tax period covers a period of less than 12 months, the net rent paid for the short tax period must be annualized. If the rental term is for less than 12 months, the rent must not be annualized beyond its term. Rent will not be annualized because of the uncertain duration when the rental term is on a month-to-month basis. "Rent" is the actual sum of money or other consideration payable directly or indirectly, by the taxpayer or for its benefit for the use of the property and includes:

- (1) Any amount payable for the use of real or tangible personal property, or any part thereof, whether designated as a fixed sum of money or as a percentage of sales, profits or otherwise;
- (2) Any amount payable as additional rent or in lieu of rents, such as interest, taxes, insurance, repairs or any other items required to be paid by the terms of the lease or other arrangement but does not include amounts paid as service charges, such as utilities, janitor services, etc. If a payment includes rent and other charges unsegregated, the amount of rent must be determined by consideration of the relative values of the rent and the other items.

"Rent" does not include incidental day-to-day expenses such as hotel or motel accommodations, daily rental of automobiles, etc. "Rent" does not include royalties based on extraction of natural resources, whether represented by delivery or purchase. For this purpose, a royalty includes any consideration conveyed or credited to a holder of an interest in property which constitutes a sharing of current or future production of natural resources from such property, irrespective of the method of payment or how such consideration may be characterized, whether as a royalty, advance royalty, rental or otherwise. Leasehold improvements are treated as property owned by

the taxpayer regardless of whether the taxpayer is entitled to remove the improvements or of whether the improvements revert to the lessor upon expiration of the lease.

F. Effect of Accounting Method. If the taxpayer has adopted the accrual method of accounting, all compensation properly accrued will be deemed to have been paid. However, compensation may be included in the apportionment factor by use of the cash method if the taxpayer is required to report such compensation under that method for unemployment compensation purposes.

G. Base of Operations. "Base of Operations" means the taxpayer's place of business from which an employee customarily begins work or to which the employee customarily returns at some other time to receive instructions, direction, and supervision from the taxpayer or communications from customers or other persons, to replenish stock or other materials, to repair equipment, or to perform any other function necessary to the exercise of the employee's trade or profession.

H. Compensation. The term "compensation" means wages, salaries, commissions, and any other form of remuneration paid to employees for personal services. Payments made to an independent contractor or any other person not properly classifiable as an employee are excluded. Only amounts paid directly to employees are included in the apportionment factor. Amounts considered paid directly include the value of board, rent, housing, lodging, and other benefits or services furnished to an employee by the taxpayer in return for personal services provided that such amounts constitute income to the recipient under the Internal Revenue Code. Employer contributions under a qualified cash or deferred arrangement as defined in Internal Revenue Code §401(k) and employer contributions to nonqualified deferred compensation plans are generally included in the apportionment factor.

I. Employee. "Employee" means any officer of a corporation, or any individual who would be considered an employee under the common law rules governing the employer/employee relationship. Generally, an individual is considered to be an employee if the individual is included by the taxpayer as an employee for purposes of the payroll taxes imposed by the Federal Insurance Contributions Act. This presumption may be overcome by evidence provided

by a taxpayer that an individual who is included as an employee for purposes of the Insurance Contributions Act would not be an employee of the taxpayer under the usual common-law rules.

J. Independent Contractor. "Independent contractor" means any individual who performs services for a taxpayer but who is not an employee of the taxpayer, and who is not otherwise subject to the supervision or control of the taxpayer in the performance of the services.

Affiliated Businesses. The total property and payroll values of affiliated businesses must be included in the apportionment calculation. An "affiliated business" means "a member of a group of 2 or more businesses in which more than 50% of the voting stock of each member corporation . . . is directly or indirectly owned by a common owner or owners." 30-A M.R.S.A. § 5250-I(1). The affiliated business group used for credit apportionment purposes is the same group that is used to determine the "base level of employment" for businesses certified as Qualified Pine Tree Development Businesses under 30-A MRSA § 5250-O and that is used to determine eligibility for ETIF benefits under 36 MRSA § 6754. The numerator of the apportionment calculation includes all new property and payroll located in the zone (net of in-state transfers, including transfers between affiliated businesses) and the denominator includes all Maine property and payroll for the taxpayer and all affiliated businesses.

7. Partners/Members of Pass-through Entities.

For shareholders of S corporations and partners in a partnership, including members of an LLC that is treated as a disregarded entity for federal tax purposes, tax credits attributable to PTDZ qualified businesses are determined at the individual taxpayer level (or at the corporate level for corporations that are partners in a partnership). That is, the tax credit amount is based on the tax liability that is attributed to PTDZ income earned by, or distributed to, the taxpayer by the business entity.

The business entity must first determine the PTDZ credit percentage through the apportionment calculation as described above. The entity must then allocate income to its owners, shareholders, partners or members, according to their distributive share or ownership interest. The owners,

shareholders, partners or members, who have income in addition to PTDZ qualified business income must then calculate the percentage of their taxable income that is attributable to the total income that is distributed by the business entity. The income from the PTDZ business as adjusted for federal purposes and modified for Maine purposes is divided by the total Maine adjusted gross income for individuals (*see* Maine Form 1040, line 16) or total adjusted federal taxable income for corporate partners (*see* Maine Form 1120, line 5). This income ratio is multiplied by the PTDZ credit percentage as calculated by the entity. The result is the percentage of total income tax that the taxpayer may claim as a credit. (*See* examples 7 and 8 in the next section for illustrations of this calculation.)

8. Examples of Apportionment

In all the following examples, it is assumed that all expansion property and payroll is 100% qualified. The following example illustrates the available tax credit under varying circumstances.

Example #1 – A new business opens in a PTDZ

Corporation A: startup business inside a PTDZ

Corporation A applies for and receives certification as a PTDZ business and then commences qualified business activities. The application provides for investment in \$200,000 of property and \$200,000 of payroll. Since all of Corporation A's business activity is qualified, it receives a 100% income tax credit.

The following two examples illustrate the available tax credit for two identical businesses, one located initially outside a PTDZ, but inside Maine and one located in a PTDZ.

Example #2 – A Maine business located outside a PTDZ expands inside a PTDZ.

Corporation B: located in Maine, outside any PTDZ

Existing facilities: \$1,000,000 property; \$1,000,000 payroll

Corporation B applies for and receives certification for expanding into a PTDZ and engages in qualified business activity. The expansion includes \$200,000 of property and \$200,000 of payroll for total Maine

property of \$1,200,000 and Maine payroll of \$1,200,000. Since Corporation B operates in Maine outside a PTDZ, the income tax credit must be apportioned as follows:

$$(\$200,000 + \$200,000)/(\$1,200,000 + \$1,200,000) = 16.67\%$$

Corporation B's PTDZ income tax credit equals 16.67% of its total Maine tax liability, which reflects the tax liability associated with the income from the expansion.

Example #3 – Expansion of an existing business located in a PTDZ.

Corporation C: located in Maine, in an area that is designated as a PTDZ. Corporation C starts with the same amount of existing property (\$1,000,000) and existing payroll (\$1,000,000) as Corporation B in the previous example. Corporation C applies for and receives certification as a PTDZ business and engages in qualified business activity. Corporation C, like Corporation B (*see* example #2), invests \$200,000 in additional property and \$200,000 in additional payroll.

Corporation C's income tax credit, like Corporation B's, is based on 16.67% of its total Maine tax liability.

The following example illustrates the credit allowed a business with two Maine locations prior to expansion, one within a PTDZ and one outside.

Example #4 – Expansion of an existing business with operations both inside and outside a PTDZ

Corporation D: located in Maine in two sites, one of which is designated a PTDZ. The facts are the same as with Example #3, except placement of the initial property and payroll. Corporation D starts with \$500,000 of property and \$500,000 of payroll in a PTDZ and \$500,000 of property and \$500,000 of payroll in its non-PTDZ Maine location. Expansion in the PTDZ equals the \$400,000 described in Example #3. Corporation D now has \$700,000 of property and \$700,000 of payroll inside the PTDZ and \$500,000 of property and \$500,000 of payroll outside the PTDZ. Corporation D, like Corporations B and C, will also base its credit on 16.7% of its Maine tax liability.

Example #5 – A non-PTDZ Maine business expands into a PTDZ and also transfers property and payroll

Business A exists in Maine, in a non-PTDZ location. Current property and payroll are \$500,000 each. Business A, certified by DECD, expands its operations into a PTDZ and begins qualified activity. Business A transfers \$100,000 of property and \$100,000 of payroll from the existing location into the PTDZ and invests in an additional \$300,000 of property and \$300,000 of payroll. After investment, the business operations are distributed as follows:

	<u>PTDZ</u>	<u>Non-PTDZ</u>
Property	\$400,000	\$400,000
Payroll	<u>400,000</u>	<u>400,000</u>
Total	\$800,000	\$800,000

At first glance, it appears as though Business A should receive a 50% income tax credit, since half of its operations are located in a PTDZ and half are located outside the zone. However, since some property and payroll were transferred to the PTDZ, the numerator of the apportionment calculation must be adjusted by subtracting out the value of the transferred property and payroll. After elimination of the transfers, the calculation looks like this:

$$(\$300,000 + \$300,000)/(\$800,000 + \$800,000) = \$600,000/\$1,600,000 = \underline{0.375 \text{ or } 37.5\%}$$

The percentage of Business A's credit is 37.5% of its Maine tax liability.

Example #6 – A non-PTDZ business with an affiliate expands into a PTDZ and also transfers property and payroll

Assume the same facts as in example #5, except that Business A also owns Business B. Business B has \$100,000 of property and \$100,000 of payroll, all in Maine, but not in a PTDZ. Business A will have to include all of Business B's payroll and property in the apportionment denominator. Business A's apportionment percentage now looks like this:

$$(\$300,000 + \$300,000)/(\$900,000 + \$900,000) = \$600,000/\$1,800,000 = \underline{0.333 \text{ or } 33.3\%}$$

Business A will get a credit for 33.3% of the combined Maine income tax liability of Business A and Business B.

Example #7 – Individual member of a pass-through entity

Individual A is a 50% owner of S corporation #1 that qualifies for a 100% PTDZ credit. Individual A has \$30,000 of income from S corporation #1 and \$40,000 of income from other sources. Individual A has no federal adjustments or Maine modifications. S corporation #1 passes 100% of the income tax credit to its shareholders, including Individual A. Individual A then calculates his/her apportionment factor as follows:

Credit from S corporation #1 = 100% of Maine tax liability related to S corporation #1

Apportionment = Individual A's income from S corporation #1/ Individual A's total Maine adjusted gross income

$$= \$30,000/(\$30,000 + \$40,000) = \$30,000/\$70,000 = \underline{0.4286 \text{ or } 42.86\%}$$

Individual A may claim 42.86% of his/her total Maine income tax liability for the year as a credit.

9. Annual Reporting Requirements as set forth in DECD Rule 19-100 §7(2)

Certified Business Information Required

A certified Pine Tree Development Zone business shall submit to DECD by March 31st of each year following its certification, a report containing the following information:

- A. A brief description of its business activities conducted within the zone during the prior calendar year;

- B. The number and location, and average wages of all full-time and part time employees employed by the business, including its affiliates, within the state as of the preceding December 31st;
- C. The number and location, average wages and benefits offered of all full-time and part time employees employed by the business within the Pine Tree Zone as of the preceding December 31st; and
- D. The value of investments made in buildings and/or facilities, business equipment and employee training within the zone during the prior calendar year.

Maine Revenue Services will review this information and any other required information and determine if the business continues to meet the requirements for a “qualified Pine Tree Development Zone business.”